



THE CHAIRMAN

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

December 4, 2000

The Honorable John D. Dingell
Ranking Member
Committee on Commerce
2322 Rayburn House Office Building
U.S. House of Representatives
Washington, DC 20515-6115

Dear Congressman Dingell:

In September 1998, you asked the Commission to provide you with annual progress reports, through the year 2003, on SEC and industry initiatives to improve corporate bond transparency. Today, I am pleased to provide this third in a series of annual reports, prepared by the Division of Market Regulation, on corporate bond transparency.

I appreciate your interest in this issue. Please do not hesitate to call me or Annette L. Nazareth, Director, Division of Market Regulation, at 202/942-0090, if we can be of further assistance.

Sincerely,


A handwritten signature in dark ink, appearing to be "AL", is written over the printed name.

Arthur Levitt

enclosure

MEMORANDUM

TO: Chairman Levitt

FROM: Annette L. Nazareth 

RE: Corporate Bond Transparency

DATE: November 27, 2000

In September 1998, in connection with your call for improved transparency in the corporate bond market, Congressman John Dingell asked the Commission to submit annual progress reports to the Commerce Committee regarding corporate bond transparency. These reports, to be provided through the year 2003, are to contain a discussion of regulatory and industry initiatives in this area to permit the Committee to determine how much progress has been made.

As we reported last year, in October 1999 the National Association of Securities Dealers, Inc. ("NASD") filed with the Commission a proposal requiring its members to report transaction information on specified U.S. corporate bonds. The proposal also provided for the establishment of a Nasdaq-operated facility, called TRACE, to facilitate the comparison, reporting, and clearance and settlement of these trades. The Commission published the proposal for public comment in December 1999. The Commission received 39 comment letters in response to the proposal.

Although the comment letters generally supported the objective of enhanced price transparency in the corporate debt markets, they raised a number of specific concerns. First, several letters expressed a concern that immediate dissemination of transaction information for corporate bonds could adversely affect the liquidity of the market. Second, commenters stated that operation of the system by Nasdaq could unfairly prevent private data vendors from providing competing services for the collection of corporate bond data. Finally, several letters urged that the comparison feature of the system be made voluntary.

Staff from the Commission's Division of Market Regulation has worked with the NASD and the industry to resolve these outstanding issues. On November 17, 2000 the NASD filed an amendment to its proposal to address some of these concerns. We published notice of this amendment for comment on November 24, 2000.¹

¹ See Securities Exchange Act Release No. 43616 (November 24, 2000). We expect publication of the notice to appear in the Federal Register during the week of November 27, 2000.

Another development that may affect transparency of the debt market is the growing number of alternative trading systems available to trade debt instruments. These alternative trading systems are subject to Reg ATS. During the past year, we have witnessed a dramatic increase in the number of ATSs trading debt securities. Just one year ago, 15 systems (out of the 37 total systems that had filed Form ATS) traded debt instruments. Currently, 34 systems trade some form of debt security, an increase of 127% in one year.

We have witnessed growth not only in the number of debt systems, but also in the different types of debt instruments traded through these systems. For example, we are seeing more systems that trade municipal securities. In addition, there are more systems that trade structured products, such as mortgage-backed and asset-backed securities. Finally, we are also seeing an increase in the number of systems that trade convertible and non-convertible corporate bonds, both investment grade and non-investment grade.

On a related issue, there has been significant progress in the last year with regard to transparency in the municipal securities market. Currently, the Municipal Securities Rulemaking Board ("MSRB") produces three transaction reports for municipal securities: the Daily Transaction Report, the Combined Daily Report, and the Inter-Dealer Report. The Daily Transaction Report, issued since January 2000, contains details on individual transactions in frequently traded municipal securities. (An issue that trades at least four times on a business day is considered to be frequently traded.) The Combined Daily Report and Inter-Dealer Report, issued since 1998 and 1995 respectively, each provide daily high, low, and average prices for frequently traded municipal securities. All of these reports are produced and made available on the next business day.

In October 2000, the Commission approved a new transaction report that will provide additional information about the municipal securities market. The new Comprehensive Transaction Report will provide information on all individual municipal securities transactions – not just frequently traded issues. According to the MSRB, investors will now have access to three times as many transactions as are included in the current daily transaction reports. The report, which will be distributed once a month, will provide such information as the trade date, CUSIP number of the issue traded, a description of the issue, the par value traded, the time of the trade reported by the dealer, the price of the transaction, and the reported yield of the transaction. Like the current Daily Transaction Report, each transaction will be categorized as either a sale by a dealer to a customer, a purchase from a customer, or an inter-dealer trade.